UNIVERSITY OF CONNECTICUT HEALTH CENTER
JOHN DEMPSEY HOSPITAL (21002 FUND)

Financial Statements
(With Management's Discussion and Analysis)

June 30, 2011 and 2010

(With Independent Auditors' Report Thereon)

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The following discussion and analysis provides an overview of the financial position and activities of the University of Connecticut Health Center John Dempsey Hospital (21002 Fund) (the Hospital) as of and for the years ended June 30, 2011, 2010, and 2009. This discussion has been prepared by management and should be read in conjunction with the financial statements and the notes thereto, which follow this section.

Through the Hospital (a licensed acute care hospital with a certified 224 bed inpatient facility; 204 general acute care beds, and 20 nursery beds), the University of Connecticut Health Center provides specialized and routine inpatient and outpatient services. The Hospital also provides comprehensive healthcare services for Connecticut's incarcerated inmates through a contract with the Correctional Managed Health Care (CHMC) program. The Hospital has long been regarded as the premier facility in the region for neonatal intensive care and high-risk maternity. It also is recognized for its cardiovascular program (interventional cardiology and surgery), cancer, musculoskeletal, and behavioral mental health services which include geriatric as well as locked inpatient psychiatric units, ambulatory partial hospitalization, and outpatient treatment programs. Additionally, the Hospital is home to the only Emergency Department in Connecticut's fast-growing Farmington Valley.

Overview of the Financial Statements

This annual report consists of management's discussion and analysis and the financial statements. The basic financial statements (statements of net assets, statements of revenues, expenses, and changes in net assets, and statements of cash flows) present the financial position of the Hospital at June 30, 2011 and 2010, and the results of its operations and its financial activities for the years then ended. These financial statements report information about the Hospital using accounting methods similar to those used by private-sector companies. The statements of net assets include all of the Hospital's assets and liabilities. The statements of revenues, expenses, and changes in net assets reflects the year's activities on the accrual basis of accounting, i.e., when services are provided or obligations are incurred, not necessarily when cash is received or paid. These financial statements report the Hospital's net assets and how they have changed. Net assets (the difference between assets and liabilities) is one way to measure financial health or position. The statements of cash flows provide relevant information about each year's cash receipts and cash payments and classifies them as to operating, investing, and capital and related financing activities.

Financial Highlights

Hospital discharges decreased 257 cases to 9,256 from fiscal 2010 to fiscal 2011. Outpatient visits increased by 5,317, or 1.5%, from the prior year. The Hospital was significantly affected by increases in staffing costs as represented by salaries and internal contractual support.

Continued focus on revenue enhancement and cost containment strategies resulted in improvement of the Hospital's operating indicator. The Hospital finished the year with an operating loss of $16.6 million compared to an operating loss of $24.3 million in the prior year. These losses were offset by non-operating revenue of $13.9 million and $14.1 million in fiscal year 2011 and 2010, respectively. Non-operating revenue included $13.5 million in state appropriations for fiscal year 2011 and 2010. The Hospital also received transfers from the Health Center of $5.4 million and $19.5 million in 2011 and 2010, respectively, resulting in changes to net assets of $2.6 million and $9.3 million. Current year transfers were made up primarily of $5 million in fringe recovery related to support services paid against the institutions general fund allotment. The Hospital's financial position at June 30, 2011, included assets of approximately $112.2 million and liabilities of approximately $44.2 million.

Net assets, which represent the residual interest in the Hospital's assets after liabilities are deducted, increased approximately $2.6 million to $68 million.

Changes in net assets represent the activity of the Hospital, resulting from revenues, expenses, gains, and losses, and are summarized for the years ended June 30, 2011, 2010, and 2009, including other changes in net assets, as follows:

	2011	2010	2009
		(In thousands)	
Summary of assets and liabilities at June 30:			
Current assets	$ 56,504	$ 53,156	$ 53,875
Assets limited as to use, net of current portion	—	—	18,879
Other assets	623	613	601
Capital assets, net	55,078	54,712	59,574
Total assets	$ 112,205	$ 108,481	$ 132,929
Current liabilities	$ 35,454	$ 33,538	$ 47,936
Long term debt excluding current installments	415	1,246	2,076
Capital lease liabilities, net of current portion	472	1,087	2,318
Accrued compensated absences, net of current portion	7,828	7,203	6,224
Estimated malpractice costs, net of current portion	—	—	18,315
Net assets restricted for research and education	67	148	144
Unrestricted net assets	15,223	14,942	3,550
Invested in capital assets, net of related debt	52,746	50,317	52,366
Total liabilities and net assets	$ 112,205	$ 108,481	$ 132,929
Summary of revenues, expenses, and transfers for the year ended June 30:			
Operating revenues	$ 266,288	$ 247,237	$ 250,309
Operating expenses	(282,919)	(271,527)	(265,782)
Operating loss	(16,631)	(24,290)	(15,473)
Nonoperating revenue , net	13,853	14,122	3,944
Loss before transfers	(2,778)	(10,168)	(11,529)
Net asset transfers	5,407	19,516	14,900
Increase in net assets	$ 2,629	$ 9,348	$ 3,371

(Continued)

Capital Assets

At June 30, 2011, the Hospital had plant and equipment of $193.4 million before accumulated depreciation compared to $187.1 million at June 30, 2010, as shown in the table below:

	2011	2010	2009
		(In thousands)	
Land	$ 183	$ 183	$ 183
Construction in progress	7,170	6,030	5,578
Buildings	100,286	98,454	97,404
Equipment	71,941	68,630	66,609
Capital leases	13,776	13,776	13,776
	$ 193,356	$ 187,073	$ 183,550

The Hospital's fiscal 2012 capital budget projects spending at approximately $9.7 million on various capital improvement projects. More detailed information about the Hospital's plant and equipment is presented in note 5 to the financial statements.

Statements of Cash Flows

The statements of cash flows provide additional information about the Hospital's financial results by reporting the major sources and uses of cash. A summary of the statements of cash flows for the years ended June 30, 2011, 2010, and 2009 is as follows:

	2011	2010	2009
		(in thousands)	
Cash received from operations	$ 274,112	$ 257,336	$ 250,009
Cash expended for operations	(276,774)	(297,883)	(247,799)
Net cash (used in) provided by operations	(2,662)	(40,547)	2,210
Net cash (used in) provided by investing activities	(9,865)	20,116	(13,047)
Net cash provided by noncapital financing activities	14,003	14,348	4,100
Net cash provided by capital and related financing activities	101	6,083	6,737
Net change in cash	$ 1,577	$ —	$ —

Significant Variances in Financial Statements

In this section, the Hospital explains the reasons for those financial statement items with significant variances relating to fiscal 2011 amounts, compared to fiscal 2010.

Summary of Assets and *Liabilities*

Changes in assets are comprised of the following:

> *Cash* – increased from an overdraft position in 2010 to $1.6 million positive cash position; attributed in part to the $13.5 million state appropriation. The Hospital expects to receive this appropriation again in fiscal year 2012.
>
> *Prepaid* – increased from June 30, 2010 to June 30, 2011 by approximately $590,000 or 19.4%. As a result of the new financial reporting system going live in July 2011 several expenses such as rent and affiliation dues were prepaid to avoid potential untimely payments. This is not expected to recur in fiscal year 2012.

Changes in liabilities are comprised of the following:

> *Accounts payable and accrued expenses* – decreased from June 30, 2010 to June 30, 2011 by approximately $2.4 million or 21.5%. This represents pay down of vendor balances prior to going live with the new purchasing/payables system.
>
> *Due to/from third-party payors* – increased from June 30, 2010 to June 30, 2011 by approximately $6.6 million or 232.3%. The change related to estimated settlements. These amounts are the result of Management's analysis of outstanding Medicare and Medicaid cost reports and other potential settlement of claims with HMO's.
>
> *Capital Leases* – decreased from June 30, 2010 to June 30, 2011 by approximately $1.2 million or 53.1%. The decrease is the result of the Hospital's repayment of current year lease obligation installments and final payments on two leases.

Summary of Revenues, Expenses, and Changes in Net Assets

> *Operating revenue* – increased from June 30, 2010 to June 30, 2011 by approximately $19 million or 7.7%. Net patient revenue went up $18.2 million or 7.4% as a result of rate increases. Contract and other revenue increased by approximately $900,000 or 80.7%; which was driven by increases in amounts received from dental and perfusion agreements with outside organizations.
>
> *Operating expenses* – increased from June 30, 2010 to June 30, 2011 by approximately $11.4 million or 4.2%, primarily due to increases in salary, fringe benefits and malpractice costs.
>
> *State appropriations* – remained at $13.5 million for June 30, 2011and 2010, due to funding from Public Act 09-3 regarding in-kind fringe benefit; the Hospital expects the same funding for fiscal year 2012.

(Continued)

Transfer from Health Center – decreased from June 30, 2010 to June 30, 2011 by approximately $14.1 million or 72.3%, primarily because the June 30, 2010 operating loss was not funded by the Health Center, in fiscal year 2011 as was done for the June 30, 2009 loss in fiscal year 2010.

FY 2012 Outlook:

As we look forward to fiscal year 2012, the Hospital's main concern focuses on maintaining outstanding clinical care while readying for changes resulting from the state's Bioscience Connecticut initiative, healthcare reform, and changes in the US and global economic environments. Average daily census at the Hospital finished slightly below budget while outpatient visits were 6% higher than budget. Management is addressing concerns on inpatient volume via its clinically focused advertising campaigns and has been encouraged by the results of increased recruiting efforts in core areas such as surgery, orthopedics and dermatology.

On July 8, 2011, the State passed Public Act 11-75 An Act Concerning the University of Connecticut Health Center (Bioscience Connecticut). The bill formalized and amended plans established by the State to establish the UConn Health Network. The new act still calls for partnership with area hospitals aimed at creating jobs and improving access to quality health care in the state. The centerpiece of the partnership remains a new patient care tower and renovations to John Dempsey Hospital at the Health Center. The plan will also include increased classroom and lab space for more medical and dental students aimed at alleviating an expected shortage of doctors and dentists in the state. Bioscience Connecticut involves the cooperation of all the area hospitals including Hartford Hospital, St. Francis Hospital and Medical Center, Connecticut Children's Medical Center, and other health care facilities and providers.

The plan is estimated to cost $661 million and includes $592 million in borrowing, $338 million previously approved. The Health Center is required to contribute $69 million raised through operations or philanthropy. Features of the Bioscience Connecticut include:

1. **Encouraging Job Growth Through Clinical Collaboration:** Local and state-wide health care organizations will collaborate on clinical and translational sciences to achieve breakthrough successes and drive the bioscience industry in the State thereby creating long term jobs.

2. **Neonatal Intensive Care Unit:** The operations will be managed by Connecticut Children's Medical Center. Patients will continue to be treated at the Health Center; some NICU physicians and all staff will remain Health Center employees. A Certificate of Need application was filed and approved for the transfer.

3. **Nationally recognized cancer center:** The goal will be to achieve National Institutes of Health designation as a Comprehensive Cancer Center, making it the second in the state.

4. **Regional Simulation Center:** It will train up to 2,000 medical practitioners each year on newest equipment and technology in simulated care settings and will be located at Hartford Hospital.

5. **Primary Care Institute:** It will be located at St. Francis Hospital and will develop new models of chronic disease management and primary care delivery and education. It will also serve to address the impending shortage of primary care providers in Connecticut.

6. **Health Disparities Institute:** It will promote enhanced healthcare research, training and delivery to minority communities.

7. **Institute for Clinical and Translational Sciences:** It will be a super-site by network partners and will speed lab-to-bedside clinical trials and breakthrough medicine.

8. **Bioscience Enterprise Zone:** It will offer state tax breaks to private companies that create jobs and work with UConn Health Network partners.

Contacting the Hospital's Financial Management

This financial report provides the reader with a general overview of the Hospital's finances and operations. If you have questions about this report or need additional financial information, please contact the Office of Chief Financial Officer, University of Connecticut Health Center, Farmington, Connecticut 06030-3800.

KPMG LLP
One Financial Plaza
755 Main Street
Hartford, CT 06103

Independent Auditors' Report

Joint Audit and Compliance Committee of the
University of Connecticut Health Center:

We have audited the accompanying statements of net assets of University of Connecticut Health Center, John Dempsey Hospital (21002 Fund) (the Hospital), an enterprise fund of the State of Connecticut, as of June 30, 2011 and 2010, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of University of Connecticut Health Center, John Dempsey Hospital (21002 Fund) as of June 30, 2011 and 2010, and the results of its operations and changes in net assets, and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Management's Discussion and Analysis (MD&A) on pages 1 to 7 is not a required part of the basic financial statements of University of Connecticut Health Center, John Dempsey Hospital (21002 Fund) but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

November 29, 2011

UNIVERSITY OF CONNECTICUT HEALTH CENTER
JOHN DEMPSEY HOSPITAL (21002 FUND)

Statements of Net Assets

June 30, 2011 and 2010

Assets	**2011**	**2010**
Current assets:		
Cash	$ 1,577,178	$ —
Patient accounts receivable, net of estimated uncollectibles of $22,321,000 and $24,399,000 at June 30, 2011 and 2010, respectively	30,512,285	29,752,888
Due from other State and Health Center agencies	12,999,560	12,789,049
Inventory	7,348,436	7,090,582
Contract and other receivables	431,489	477,986
Prepaid expenses	3,634,955	3,045,246
Total current assets	56,503,903	53,155,751
Noncurrent assets:		
Other assets	623,030	613,242
Capital assets, net (note 5)	55,078,415	54,711,812
Total noncurrent assets	55,701,445	55,325,054
Total assets	$ 112,205,348	$ 108,480,805
Liabilities and Net Assets		
Current liabilities:		
Cash overdraft	$ —	$ 3,082,016
Accounts payable and accrued expenses	8,760,603	11,160,327
Accrued payroll	7,112,987	6,506,559
Due to State of Connecticut	3,261,633	2,888,485
Due to third-party payors	9,415,877	2,833,399
Accrued compensated absences, current portion (note 6)	5,458,013	5,005,189
Long-term debt, current installments (note 6)	830,396	830,396
Capital leases, current portion, (note 6)	614,731	1,231,751
Total current liabilities	35,454,240	33,538,122
Noncurrent liabilities:		
Accrued compensated absences, net of current portion (note 6)	7,827,458	7,202,589
Long-term debt, excluding current installments (note 6)	415,198	1,245,595
Liabilities under capital leases, net of current portion (note 6)	471,882	1,086,613
Total noncurrent liabilities	8,714,538	9,534,797
Total liabilities	44,168,778	43,072,919
Net assets:		
Invested in capital assets, net of related debt	52,746,208	50,317,457
Restricted for research and educational	67,124	148,123
Unrestricted	15,223,238	14,942,306
Total net assets	68,036,570	65,407,886
Total liabilities and net assets	$ 112,205,348	$ 108,480,805

See accompanying notes to financial statements.

UNIVERSITY OF CONNECTICUT HEALTH CENTER
JOHN DEMPSEY HOSPITAL (21002 FUND)

Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2011 and 2010

	2011	2010
Operating revenues:		
Net patient service revenues (note 4)	$ 264,332,834	$ 246,155,547
Contract and other revenues	1,954,663	1,081,457
Total operating revenues	266,287,497	247,237,004
Operating expenses:		
Salaries and wages	95,631,329	88,764,151
Fringe benefits	42,155,396	38,825,799
Medical/dental house staff	16,188,925	15,292,507
Medical contractual support	3,480,635	3,203,566
Internal contractual support	17,136,316	16,645,836
Outside agency per diems	1,650,395	1,931,044
Depreciation and amortization	9,298,913	10,571,031
Loss on disposal	199,767	13,970
Pharmaceutical/medical supplies	51,662,400	50,645,210
Utilities	2,780,030	2,668,129
Outside and other purchased services	29,007,441	29,950,586
Insurance	4,458,366	3,357,735
Repairs and maintenance	6,276,935	6,153,452
Other expenses	2,992,043	3,504,128
Total operating expenses	282,918,891	271,527,144
Operating loss	(16,631,394)	(24,290,140)
Nonoperating revenues (expenses):		
Gift income	502,896	847,835
State appropriations	13,500,000	13,500,000
Interest income	74	49,785
Interest expense	(149,794)	(275,340)
Net nonoperating revenues	13,853,176	14,122,280
Loss before transfers	(2,778,218)	(10,167,860)
Transfer from Health Center - unrestricted (note 7)	5,406,902	19,515,386
Increase in net assets	2,628,684	9,347,526
Net assets, beginning of year	65,407,886	56,060,360
Net assets, end of year	$ 68,036,570	$ 65,407,886

See accompanying notes to financial statements.

UNIVERSITY OF CONNECTICUT HEALTH CENTER
JOHN DEMPSEY HOSPITAL (21002 FUND)

Statements of Cash Flows

Years ended June 30, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Cash received from patients and third-party payors	$ 272,110,578	$ 255,677,804
Cash received from contract and other revenue	2,001,160	1,658,350
Cash paid to employees for salaries and fringe benefits	(139,843,994)	(118,238,424)
Cash paid for other than personal services	(136,929,206)	(179,645,214)
Net cash used in operating activities	(2,661,462)	(40,547,484)
Cash flows from investing activities:		
Malpractice trust fund	—	25,789,282
Investment income	74	49,785
Additions to property and equipment, net	(9,865,283)	(5,723,019)
Net cash (used in) provided by investing activities	(9,865,209)	20,116,048
Cash flows from noncapital financing activities:		
Gifts received	502,896	847,835
State appropriations	13,500,000	13,500,000
Net cash provided by noncapital financing activities	14,002,896	14,347,835
Cash flows from capital and related financing activities:		
Interest paid	(161,785)	(268,352)
Transfer from Health Center	5,406,902	19,515,386
Net repayments on cash overdraft	(3,082,016)	(10,349,923)
Repayment of long-term debt	(2,062,148)	(2,813,510)
Net cash provided by capital and related financing activities	100,953	6,083,601
Net change in cash	$ 1,577,178	$ —
Reconciliation of operating loss to net cash (used in) provided by operating activities:		
Operating loss	(16,631,394)	(24,290,140)
Adjustments to reconcile operating loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	9,298,913	10,571,031
Loss on disposal	199,767	13,970
Changes in operating assets and liabilities:		
Patients accounts receivable, net	(759,397)	4,012,110
Due from other State and Health Center agencies	(210,511)	(12,540,207)
Inventory	(257,854)	(1,185,991)
Contract and other receivables	46,497	576,893
Prepaid expenses	(589,709)	269,616
Due from third-party payors, net	6,582,478	5,510,147
Other assets	(9,788)	(12,097)
Accounts payable and accrued expenses	(2,387,733)	1,103,710
Due to other State and Health Center agencies	373,148	(9,862,771)
Accrued payroll	606,428	46,406
Accrued compensated absences	1,077,693	464,839
Estimated malpractice costs	—	(15,225,000)
Net cash used in operating activities	$ (2,661,462)	$ (40,547,484)

See accompanying notes to financial statements.

(1) Description of Reporting Entity and Summary of Significant Accounting Policies

(a) Reporting Entity

The financial statements include those asset, liability, revenue, and expense accounts reflected in the accounting records of the John Dempsey Hospital (the Hospital) including the Dental Clinics, and the University of Connecticut Health Center's malpractice self-insurance fund (which was transferred to the Health Center in 2011), which are primarily accounted for in the 21002 Fund of the University of Connecticut Health Center (the Health Center). There are 21 members of the Board of Trustees. Five serve as ex officio, voting members by virtue of other positions: The Governor is President of the Board, the Commissioners of Agriculture, Education, and Economic and Community Development are Board members, and the Chair of the Health Center Board of Directors is a member. Two Board members are elected by alumni for four-year terms (and may be re-elected once, in succession). One undergraduate student is elected by undergraduates for a two-year term. One graduate or professional student is elected by graduate and professional students for a two-year term. Twelve members are appointed by the Governor, subject to confirmation by the General Assembly, for six-year terms, and may be reappointed without limit.

There are 18 members of the University of Connecticut Health Center Board of Directors. Three serve as ex officio voting members and serve concurrently with their positions: The Commissioner of Public Health, The Secretary or a designated under-secretary of the Office of Policy and Management and the President of the University. All other terms are for three years and include: three members appointed by the Governor, three members appointed by the chair of the Board of Trustees (two of which must be members of the Board of Trustees and last who serves at the chair of the Board of Directors), and 9 at-large members appointed by the Board of Directors itself.

Reference is made to note 7 for related party transactions.

The Hospital is an enterprise fund of the State of Connecticut ("the State") and is therefore generally exempt from federal income taxes under Section 115 of the Internal Revenue Code of 1986.

The Finance Corporation was established pursuant to Public Act No 87-458. The purpose of the Finance Corporation is to provide greater flexibility for the Hospital and to promote the more efficient provision of health care services. As such, the Finance Corporation has been empowered to purchase supplies and equipment, acquire facilities, approve write-offs of Hospital accounts receivable, process malpractice claims on behalf of the Hospital and Health Center beginning in 2011, as well as negotiate joint ventures, shared service, and other agreements for the benefit of the Hospital.

(b) Basis of Presentation

The Hospital's financial statements are prepared in accordance with all relevant Governmental Accounting Standards Board (GASB) pronouncements. GASB No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting,* states that proprietary activities may elect to apply the provisions of Financial

Accounting Standards Board (FASB) pronouncements issued after November 30, 1989 that do not conflict with or contradict GASB pronouncements. The Health Center has not made this election.

The Hospital has adopted Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments,* as amended by GASB Statements No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities, and No. 37, Basic Financial Statements – and Management Discussion and Analysis – for State and Local Governments: Omnibus,* as of July 1, 2001.

John Dempsey Hospital also adopted GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, as of July 1, 2001. These GASB pronouncements established financial reporting standards for state and local governmental entities, including net asset presentation, certain classifications of revenues and expenses and management's discussion and analysis.

(c) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingencies at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Financial statement areas where management applies the use of estimates consist primarily of the allowance for uncollectible accounts, and third-party reimbursement reserves.

(d) Proprietary Fund Accounting

The Hospital utilizes the proprietary fund method of accounting whereby revenue and expenses are recognized on the accrual basis. All revenues and expenses are subject to accrual.

(e) Cash and Cash Overdraft

Cash includes cash in banks. Cash overdraft positions, which occur when total outstanding issued checks exceed available cash balances at the end of each reporting period, are presented as a liability within the statement of assets. See note 2 for discussion regarding the Hospital's available borrowing.

(f) Accounts Receivable and Net Patient Service Revenues

Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Settlements are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

(g) Contract and Other Revenues

Contract and other revenues primarily consist of net receipts resulting from contractual revenue with area hospitals.

(h) Capital Assets

Property and equipment acquisitions are recorded at cost. Betterments and major renewals are capitalized, and maintenance and repairs are expensed as incurred.

Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. Buildings have an estimated useful life of 5 to 50 years and equipment has an estimated useful life of 2 to 25 years. Assets acquired under capital leases and leasehold improvements are depreciated no longer than the lease term.

(i) Inventory

Inventory is recorded at cost, being determined by the first-in, first-out (FIFO) method. Short-term or minor supplies are expensed as incurred.

(j) Fair Value of Financial Instruments

Assets and liabilities such as accounts receivable, contract and other receivables, cash overdraft, accounts payable and accrued expenses and accrued payroll, the carrying amount approximates fair value because of the short maturity of these instruments.

(k) Retirement Plans

Eligible Hospital employees, as defined, may participate in the following State of Connecticut retirement plans: the State Retirement System Tier I, Tier II, Tier IIa, and the Teachers' Retirement System defined benefit plans; and the Alternate Retirement Plan which is a defined contribution plan. These plans are funded by contributions from the State as well as payroll deductions from employees, except for the Tier II Plan, which is noncontributory.

In addition, eligible employees may participate in a State of Connecticut defined contribution deferred compensation plan, which is funded by payroll deductions from employees.

In 2008, the State of Connecticut implemented Government Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The State provides post retirement health care and life insurance benefits to eligible Health Center employees, including those of John Dempsey Hospital, in accordance with Sections 5-257(d) and 5-259(a) of the Connecticut General Statutes. Upon retirement, liability for retirement and other benefits rests with the State of Connecticut. Therefore, the liability is reported by the State of Connecticut and not recognized in the financial statements of the Hospital. When employees retire, the State pays up to 100% of their health care insurance premium cost (including the cost of dependent coverage). The State finances the cost of post retirement health care and life insurance benefits on a pay-as-you-go basis through an appropriation in the General Fund.

Information is not available from the State of Connecticut specifically allocating pension benefits; plan assets, obligations, and expenses applicable to employees of the Hospital. (Reference is also made to note 6).

(l) Compensated Absences

The Hospital's employees earn vacation, personal, compensatory and sick time at varying rates depending on their collective bargaining units. Employees may accumulate sick leave up to a specified maximum. Employees are not paid for accumulated sick leave if they leave before retirement. However, employees who retire from the Hospital may convert accumulated sick leave to termination payments at varying rates, depending on the employee's contract. Amounts recorded on the statements of net assets are based on historical experience. All other compensated absences are accrued at 100% of their balance. Compensated absences have been allocated between current and noncurrent based on historical information.

(m) Third Party Payors

Laws governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. Each year as the Office of Inspector General's (OIG) work plan changes, new areas of scrutiny surface. As a result, there is at least a reasonable possibility that recorded estimates will change by a material amount in any given period.

(n) Medical Malpractice

Health care providers and support staff of the Hospital are fully protected by State statutes from any claim for damage or injury, not wanton, reckless or malicious, caused in the discharge of their duties or within the scope of their employment (statutory immunity). Any claims paid for actions brought against the State as permitted by waiver of statutory immunity have been charged against the Health Center's malpractice self-insurance fund. Prior to 2011 the malpractice trust fund was controlled by John Dempsey Hospital, which annually retained a qualified actuary to assist with calculating and determining the appropriate malpractice reserve. The calculated actuarial reserve was also equally funded as was required by Section 10a-256 (the public act that established the malpractice trust fund). As more fully described in note 8, in 2010, the State of Connecticut passed Public Act No. 09-3, which resulted in control of the fund being transferred from the Hospital to the Health Center. As a result of the transfer, the Health Center now allocates an annual malpractice premium to John Dempsey Hospital, designed to reflect an estimate for the current year's cash claims to be processed. For the years ended June 30, 2011 and 2010 such premiums were $4,145,224 and $3,064,018, respectively. These premiums are included in the Hospital's statements of revenues, expenses, and changes in net assets as insurance expense.

(o) Net Assets

Net assets of the Hospital are classified in three components. Net assets invested in capital assets net of related debt, consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase on construction of those assets. Expendable funds for research and education represent balances held for use in promoting various Hospital initiatives. All other assets are classified as unrestricted net assets.

(p) Regulatory Matters

The Hospital is required to file semi-annual and annual operating information with the State of Connecticut Office of Health Care Access (OHCA) and is required to file annual cost reports with Medicare and Medicaid.

(2) Hypothecation

In accordance with State Statute, John Dempsey Hospital can borrow from the State up to 90% of its net patient receivables, contract and other receivables to fund operations. As of June 30, 2011 and 2010, the Hospital had drawn down $-0- and $3,082,016, respectively. As of June 30, 2011 and 2010, the Hospital has available $27,849,397 and $24,125,771, respectively, under the State Statute.

(3) Charity Care

The Hospital maintains records to identify and monitor the level of charity care it provides. These records include the amount of charges forgone for services and supplies furnished under its charity care policy, the estimated cost of those services and supplies, and equivalent service statistics. During 2011 and 2010, the Hospital provided charity care services of $912,282 and $1,013,714, respectively. The cost basis of these services was $480,274 and $511,090, respectively. No net patient service revenue was recorded for these services and expenses associated with these services were included in operating expenses.

(4) Net Patient Service Revenues

The Hospital provides health care services primarily to residents of the region. Revenues from the Medicare programs accounted for approximately 40% and 37% of the Hospital's net patient service revenues for the years ended June 30, 2011 and 2010, respectively. Revenues from the Medicaid programs accounted for approximately 29% and 27% of the Hospital's net patient service revenues for the years ended June 30, 2011 and 2010, respectively. Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation. The Hospital believes that it is in compliance with all applicable laws and regulations and is not aware of any pending or threatened investigations involving allegations of potential wrong doing. While no such regulatory inquiries are outstanding, compliance with such laws and regulations can be subject to future government review and interpretation as well as significant regulatory action including fines, penalties, and exclusion from the Medicare and Medicaid programs. Changes in the Medicare and Medicaid programs and the reduction of funding levels could have an adverse impact on the Hospital.

Patient accounts receivable included approximately 32% and 29% due from Medicare and approximately 12% and 13% due from Medicaid at June 30, 2011 and 2010.

Patient service revenue is reported net of allowances for the years ended June 30, was:

		2011		2010
Gross patient service revenue	$	543,303,930	$	514,239,006
Less contractual allowances		(275,186,908)		(260,249,422)
Less provision for bad debt		(3,784,188)		(7,834,037)
Net patient service revenue	$	264,332,834	$	246,155,547

The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. As such, gross patient revenues are reduced by contractual allowances. A summary of the payment arrangements with major third-party payors follows:

Medicare

Inpatient acute care services rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system which are based on clinical, diagnostic, and other factors. The Hospital's classification of patients under the Medicare program and the appropriateness of their admission are subject to an independent review by a peer review organization under contract with the Hospital. Services to Medicare beneficiaries are paid based on a prospective payment system (PPS) based on the classification of each case into a Diagnostic-Related Group (DRG). Inpatient psychiatric services are also reimbursed via a PPS system established for inpatient psychiatric patients based on pre-determined hospital specific per diems. The Hospital is reimbursed for Direct Graduate Medical Education and Medicare Bad Debts at an interim rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicare fiscal intermediary. The Hospital's Medicare cost reports have been audited by the Medicare fiscal intermediary through fiscal year 2007.

Medicaid

In-patient services rendered to Medicaid program beneficiaries are reimbursed, in part, under the Tax Equity and Fiscal Responsibility Act (TEFRA) reimbursement methodology which provides for a cost-based reimbursement subject to a maximum target rate amount per discharge with the exception of individuals who are eligible for care under the state managed Medicaid program where reimbursement is based on contracts with other managed care companies. The Hospital is reimbursed at an interim rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof by the Medicaid fiscal intermediary.

Outpatient services rendered to patients are reimbursed based on the cost of services provided except for individuals in the managed Medicaid program where reimbursement is based on contracts as described above. The Hospital's Medicaid cost reports have been audited by the Medicaid fiscal intermediary through 1997. Unaudited cost reports have been submitted as requested by Department of Social Services (DSS) through fiscal year 2008.

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Commercial Insurance and Managed Care

The Hospital has agreements with certain commercial insurance carriers and Health Maintenance Organizations (HMOs) to provide medical services to subscribing participants. In addition, the HMOs make fee-for-service payments to the Hospital for certain covered services based upon discounted fee schedules.

(5) Capital Assets, Net

Capital assets at June 30 consist of the following:

	2011	2010
Land	$ 183,137	$ 183,137
Construction in progress (estimated cost to complete $4.6 million)	7,169,410	6,030,347
Buildings	100,285,929	98,453,605
Equipment	71,941,150	68,629,917
Capital leases	13,776,275	13,776,275
	193,355,901	187,073,281
Less accumulated depreciation and amortization	138,277,486	132,361,469
Capital assets, net	$ 55,078,415	$ 54,711,812

Plant and equipment activity for the years ended June 30, 2011 and 2010 was as follows:

	2010	Additions	Deletions	2011
Land	$ 183,137	—	—	$ 183,137
Construction in progress	6,030,347	2,854,329	(1,715,266)	7,169,410
Buildings	98,453,605	1,832,324	—	100,285,929
Equipment	68,629,917	6,893,896	(3,582,663)	71,941,150
Capital leases	13,776,275	—	—	13,776,275
	$ 187,073,281	11,580,549	(5,297,929)	$ 193,355,901

	2009	Additions	Deletions	2010
Land	$ 183,137	—	—	$ 183,137
Construction in progress	5,577,936	2,466,871	(2,014,460)	6,030,347
Buildings	97,403,562	1,050,043	—	98,453,605
Equipment	66,608,686	4,220,565	(2,199,334)	68,629,917
Capital leases	13,776,275	—	—	13,776,275
	$ 183,549,596	7,737,479	(4,213,794)	$ 187,073,281

Related information on accumulated depreciation and amortization for the years ended June 30, 2011 and 2010 was as follows:

	2010	Additions	Deletions	2011
Buildings	$ 71,156,929	2,816,077	—	$ 73,973,006
Equipment	49,917,022	5,402,710	(3,382,896)	51,936,836
Capital leases	11,287,518	1,080,126	—	12,367,644
Total	$ 132,361,469	9,298,913	(3,382,896)	$ 138,277,486

	2009	Additions	Deletions	2010
Buildings	$ 68,317,171	2,839,758	—	$ 71,156,929
Equipment	46,119,058	5,983,328	(2,185,364)	49,917,022
Capital leases	9,539,573	1,747,945	—	11,287,518
Total	$ 123,975,802	10,571,031	(2,185,364)	$ 132,361,469

(6) Long-Term Liabilities

Long-term liability activity for the years ended June 30, 2011 and 2010 were as follows:

	June 30, 2010 balance	Additions	Reductions	June 30, 2011 balance	Amounts due within 1 year
Accrued compensated absences	$ 12,207,778	11,997,127	(10,919,434)	$ 13,285,471	$ 5,458,013
Capital leases	2,318,364	—	(1,231,751)	1,086,613	614,731
Long-term debt	2,075,991	—	(830,397)	1,245,594	830,396
Total long-term liabilities	$ 16,602,133	11,997,127	(12,981,582)	$ 15,617,678	$ 6,903,140

	June 30, 2009 balance	Additions	Reductions	June 30, 2010 balance	Amounts due within 1 year
Accrued compensated absences	$ 11,742,939	10,770,227	(10,305,388)	$ 12,207,778	$ 5,005,189
Estimated malpractice costs	25,225,000	—	(25,225,000) *	—	—
Capital leases	4,301,478	—	(1,983,114)	2,318,364	1,231,751
Long-term debt	2,906,387	—	(830,396)	2,075,991	830,396
Total long-term liabilities	$ 44,175,804	10,770,227	(38,343,898)	$ 16,602,133	$ 7,067,336

* See note 8 for additional details

Long-term debt and capital lease obligations as of June 30, 2011 and 2010 consisted of the following:

	2011	2010
Leasehold note-People's Bank, fixed rate beginning December 1, 2006 and maturing November 30, 2012 at a fixed rate of 6.35%.	$ 1,245,594	$ 2,075,991
Capital lease obligation - Citicorp Leasing, Inc. Beginning January 18, 2008. Payments of principal and interest at 2.7%, begin April 1, 2008 and continue until January 13, 2013, collateralized by financed equipment.	1,086,613	1,685,232
Capital lease obligation – GE Capital: Phillips Medical Beginning in 2005 for five years at 4.8%	—	360,698
Capital lease obligation – GE Capital: Medical Equipment Beginning in 2006 for five years at 5.2%	—	272,434
Total	2,332,207	4,394,355
Less current portion	1,445,127	2,062,147
Long-term debt, less current portion	$ 887,080	$ 2,332,208

Aggregate maturities of notes payable at June 30, 2011 were:

	Leasehold note
Fiscal year:	
2012	$ 830,396
2013	415,198
	$ 1,245,594

Aggregate maturities of capital leases at June 30, 2011 were:

		Capital leases
Fiscal year:		
2012	$	633,484
2013		475,041
Total minimum lease payments		1,108,525
Less amount representing interest		21,912
Present value of minimum lease payments	$	1,086,613

The Hospital also participates in operating lease agreements under the University for which its departments are allocated expenses based on square footage occupied. Rent expense was $2,500,888 and $2,081,928 in 2011 and 2010, respectively. Aggregate minimum lease payments for the leases are as follows:

		Amount
Fiscal year:		
2012	$	2,113,145
2013		1,937,082
2014		1,948,076
2015		1,321,564
2016		1,014,073
Thereafter		3,088,680
Total	$	11,422,620

(7) Related Party Transactions

The expenses reported in the statements of revenues, expenses, and changes in net assets do not include undetermined amounts for salaries, services, and expenses provided to and received from the Health Center and other state agencies. Complete allocations have not been made for salaries and other services incurred by the Hospital on behalf of other Health Center entities. In addition, certain activities accounted for in the 21002 Fund are periodically evaluated and transferred to/from other funds depending on the overall objectives of the Health Center.

The Hospital is party to an agreement with the Health Center whereby the salaries of certain administrative employees are reimbursed by the Hospital. The non-clinical support services provided to the Hospital from Health Center have been reported in the financials as part of the internal contractual support.

The Health Center transferred $5 million in 2011 and $4.9 million in 2010, related to fringe benefit recoveries for support services paid by the general fund. During the years ended June 30, 2011 and 2010, $400,000 and $3.7 million was transferred to fund capital projects. These transfers are reflected as a net

(Continued)

asset transfer in the statements of revenues, expenses and changes in net assets. In 2010, the Health Center transferred $11.5 million of cash to the Hospital to subsidize the prior year loss.

As more fully described in note 8, beginning in 2010, the Health Center charges the Hospital with an annual premium for medical malpractice costs which is determined by the Health Center under this self-insured program. The Hospital is not liable beyond the annual premium, but may have future operational subsidies affected by the performance of the malpractice trust fund.

As described in note 1, the Hospital participates in certain State of Connecticut retirement plans. The State charges the Hospital for these and other fringe benefits. During the years ended June 30, 2011 and 2010, the Hospital incurred $42,155,396 and $38,825,799, respectively, for employee fringe benefits. The State subsidized approximately $13.5 million of employee fringe benefits for fiscal years 2011 and 2010. Related salary costs were $95,631,329 and $88,764,151, respectively.

Contributions to the State for an assessment of postemployment benefits other than pension benefits are also included in employee benefits expense. The related accrued postemployment benefit liability is a liability of the State.

The Hospital provides medical services to correctional managed health care patients under a Health Center contract with the State of Connecticut Department of Correction (CTDOC). Revenue recorded under this contract was approximately $9,610,000 and $10,218,000 for the years ended June 30, 2011 and 2010, respectively, and is included in net patient service revenues in the statements of revenues, expenses, and changes in net assets. The Hospital also provides outpatient care to Correctional Managed Health Care patients at Medicaid rates.

In 2011 and 2010, the Hospital recorded the liability for Finance Corporation purchases directly in accounts payable and accrued expenses in the statements of net assets.

(8) Reporting of the Malpractice Trust Fund

The Health Center is self-insured with respect to medical malpractice risks. Estimated losses from asserted and unasserted claims identified under the Health Center's incident reporting system and an estimate of incurred but not reported claims are accrued based on actuarially determined estimates that incorporate the Health Center's past experience as well as other considerations, including the nature of each claim or incident and relevant trend factors. The Hospital provides timely incident reporting to the Health Center to assist the Health Center in maintaining appropriate reserve balances.

In fiscal year 2010, the State of Connecticut passed Public Act No. 09-3, *AN ACT CONCERNING EXPENDITURES AND REVENUE FOR THE BIENNIUM ENDING JUNE* 30, 2011, (Public Act) . Sec. 74. of the Public Act states "(Effective from passage) (a) Notwithstanding the provisions of section 10a-256 of the general statutes, the sum of $10,000,000 shall be transferred from The University of Connecticut Health Center Medical Malpractice Trust Fund and credited to the resources of the General Fund for each of the fiscal years ending June 30, 2010, and June 30, 2011." The Public Act also states "the amount of funding necessary to protect the Health Center for malpractice shall be determined and approved by the Board of Trustees of the University of Connecticut." Since the State effectively removed control and responsibility for maintaining and managing the malpractice fund from the Hospital, the Fund was transferred from the Hospital to the Health Center. Accordingly, beginning in 2010, the reporting of the trust fund is now reflected in the Health Center's financial statements. Also beginning in 2010, the Health Center charges each affiliate or clinical area with an annual malpractice premium that is designed to approximate the current year claim payments of the Malpractice Trust Fund. To the extent that claims for cases exceed current year premium charged by the Health Center, the Health Center may petition the State to make up the difference. The Hospital is not responsible for amounts beyond the annual premium allocated by the Health Center. However, operational subsidies from the State and/or the Health Center may be affected by the performance of the Health Center's malpractice program. In fiscal year 2011, an additional $10 million was transferred to the State of Connecticut's General Fund as required by the Public Act. At June 30, 2011 and 2010, the Health Center Malpractice Trust Fund had actuarial reserves of approximately $20.4 million and $18.3 million and assets of approximately $4.3 million and $10 million for fiscal year 2011 and 2010, respectively.

(9) Subsequent Events

The Hospital has evaluated subsequent events through November 29, 2011, which represents the date the financial statements were available to be issued and noted no subsequent events that would have impacted the Hospital's financial statements.